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From Liberalisation to Industrial Policy: Towards a Geoeconomic Turn in the European Defence Market?

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Abstract

The European defence market can be described as a geoeconomically relevant sector that forms part of Europe's overall economy, not least in the way that it is a producer of military capabilities and technologies and a repository of scientific skills. Traditionally, European Union (EU)-level steps to support and liberalise the sector have reflected a regulatory approach marked by soft law, but in recent years, the EU has also developed financial tools to incentivise defence co-operation. Looking specifically at the European Defence Fund (EDF), this article views this transition as evidence of a 'geoeconomic turn' in European defence market policy that is a response to structural challenges related to technology control, security of supply and geopolitical competition. Employing relative gains theory and liberal intergovernmentalism, this article charts the transition from market liberalisation to industrial policy in EU defence market initiatives based on specific intra- and extra-political dynamics.

Keywords: defence; European Union; geoeconomics; industry; technology

Introduction

Over the past three decades, the European Union (EU) and its member states have sought to liberalise the European defence market by developing regulations at the EU level. Recognising that market fragmentation along national lines has given rise to higher equipment costs, supply disruptions and lost research and capability development collaboration opportunities, the EU has seen market liberalisation of the defence sector as a way to develop a Single Market in defence, even if such a market still does not fully exist in the EU. Countless communications and strategies from the European Commission have argued for greater cross-border co-operation in defence between EU member states, as well as calling for non-discrimination in how European governments award procurement contracts to defence firms. Following the early development of the Common Security and Defence Policy (CSDP), the establishment of the European Defence Agency (EDA) and the steps to create a Constitution for Europe in the early 2000s, the Commission sought to develop an EU Single Market in defence by developing a 'defence package' of two directives – a process started in 2004 and finalised in 2009 – to address defence procurement and transfers of military equipment within the EU.

In both cases, regulation was aimed at removing trade barriers for military equipment between EU member states. The defence package, whilst recognising the specificities of the defence market – viz., that governments are both buyers and sellers in the market – sought to transplant the norms of the Single Market into the EU defence sector. In the early stages of the development of EU defence industrial policy, the Commission and member states were inspired by the regulation of the Single Market, but the period up

to 2009 – when the 'defence package' was developed – cannot be said to be a watershed moment. In recent years, however, the EU has shifted away from market liberalisation in defence to industrial policy where it directly uses financial resources from the EU budget to encourage defence research and capability development. In this respect, the EU has also moved away from a traditional strategy of applying soft law to the defence sector, and in 2013, the European Council and the Commission decided to specifically intervene in the European defence market with financial tools.

Indeed, after the first European Council (2013) summit on defence in December 2013, leaders took the decision to develop critical military gaps that had been neglected for years. Unlike the 2009 'defence package', the 2013 summit is far closer to a watershed moment where any pre- and post-geoeconomic turn can be discerned, not least because the summit sought to address the under-investment in defence made apparent by the 2008 financial crisis. Indeed, the 2013 Defence Summit called for common military capabilities, and the Commission and the European Parliament followed up on the European Council's wishes by developing the first-ever EU-level funding mechanism for defence research and capability development. The European Defence Fund (EDF) would not only break an important taboo about funding military programmes from the EU budget, but it would also overtly seek to support the European Defence Technological and Industrial Base (EDTIB) by producing European-made weapons systems and equipment.

In this article, we ask how and why has this shift from market liberalisation to industrial policy occurred. Here, one could point to the potential ineffectiveness of EU regulation and its failure to genuinely liberalise the European defence market (Fiott, 2023). However, this article argues that the transition from market liberalisation to industrial policy is reflective of structural changes underway in the global order including growing geopolitical competition (Lavery and Schmid, 2021). This article argues that the growth of industrial policy in the defence sector is reflective of a broader geoeconomic turn in the EU. As the introduction to this special issue makes clear, the EU is presently facing the rise of China, growing industrial competition with the United States, an increased tendency for economic interdependencies to be 'weaponised' and the greater competition over and for technologies and critical raw materials (Herranz-Surrallés et al., 2024). Indeed, the European defence market has become a key component of the Union's attempts to enhance its 'strategic autonomy' or 'sovereignty' in the field of defence, technology and industrial policy.

Geoeconomics stresses the non-military nature of international conflict where control of technology and resources and the promotion of standards are as much a part of political power as territory and military capabilities (Wigell et al., 2020). However, geoeconomics remains relevant to military power. Indeed, military power can only be achieved through economic security, and military power is a way to safeguard the technological and industrial base of a country (Baru, 2012). There is then a symbiotic rather than binary relationship between economic and military power due to industrial and technological processes (Bellais, 2023; Csurgai, 2017). This actually aligns closely with the practical realities of the European defence market where the production of military capabilities relies heavily on technological, commodity and resource inputs from the general economy (see Smith and Fontanel, 2008). Accordingly, whilst much of the scholarly attention has focused on the supposed 'geoeconomic turn' in EU trade policy (Adriaensen and Postnikov, 2022; Meunier and Nicolaidis, 2019), this article seeks to make a contribution to the role of the

defence sector in debates about the geoeconomic evolution of the EU by looking specifically at the growth of EU industrial policy in defence. The article treats the industrial policy shift in the defence sector as a core expression of the geoeconomic turn in the EU (see Herranz-Surrallés et al., 2024, fig. 1).

Unpacking our research question reveals a number of important issues that are tackled in this article. First, there is a need to explain the structural factors that have given rise to any 'geoeconomic turn' or industrial policy shift in European defence market policy. Second, it is necessary to capture how the preferences of EU member states have evolved during this geoeconomic transition. Third, one needs to better understand the role of EU institutions such as the Commission in helping to shape the geoeconomic rationale for EU defence industrial policy. To this end, this article draws on relative gains theory and liberal intergovernmentalism (LI) to explain the formation of preferences in favour of industrial policy and how member states agreed on the creation of the EDF. In doing so, the article hopes not only to better connect EU defence market policies with the literature on geoeconomics but also to make a contribution to existing theoretical debates about the EDF (Calcara, 2019a; Fiott, 2019a; Håkansson, 2021; Haroche, 2020; Hoeffler, 2023; Sabatino, 2022).

In terms of the methodology employed for this article, we will draw on primary and secondary sources such as official EU documents (communications, regulations and conclusions) and specialist academic literature. The article will also draw on nine semi-structured interviews conducted with relevant EU and government officials who are or have been involved in the development of EU defence industrial policy and/or the EDF.

I. Conceptually Understanding the 'Geoeconomic Turn' in EU Defence Industrial Policy

Although several theories of political science see 'geoeconomics' as predominantly a domain of economic and non-military forms of political conflict and contestation, there are solid grounds to analyse the European defence market from a geoeconomic perspective. Indeed, if one focuses exclusively on finished weapons systems, acquisition strategies and the military use of capabilities, one foregoes an appreciation of the economic inputs required to ensure that the defence market functions properly. Such inputs include component parts and constituent technologies that are integrated into weapons systems. The industrial processes and economic inputs required to develop weapons systems also raise questions about the critical raw material inputs needed to ensure the construction of defence capabilities (e.g., without rare earth minerals such as erbium or neodymium, it is difficult to produce precision-guided munitions or laser-guided missiles). Such critical raw materials are at risk of political instrumentalisation, as many are concentrated in the hands of a few countries such as China.

It is for such reasons that the academic literature on Europe's defence market increasingly affords attention to supply chain issues and matters of security of supply – essentially, a policy to avoid dependencies on supplies that can be instrumentalised by third states, which, in turn, can pose a security risk for the functioning and development of military capabilities. Kleczka et al. (2023) show how the participation of non-EU firms in the European defence sector highlights Europe's dependency on supply and technology

imports. In many other economic sectors, a reliance on non-EU supplies and inputs would not raise major security issues, as the proper functioning of the market is based on competition, competitive prices and Pareto efficiency between trade partners, where each gains from economic exchange. Yet, the defence market does not function in these 'proper' terms as there are many intervening variables that raise concerns for governments (Martí Sempere, 2019): for example, governments and militaries may be unwilling to exchange and share technologies with partners and rival countries, and a dependency on a technology or critical raw material may pose a strategic vulnerability in times of war.

All these issues have become apparent in the development of the EDF, which this article argues is a clear example of the EU's industrial policy and geoeconomic turn in defence. Prior to the formal creation of the Fund in 2016, the EU relied on regulation to develop soft law to guide activities on defence procurement and intra-EU weapons and equipment transfers. There were clear limits as to how far such measures could alter the European defence market (Simon, 2022). However, with the introduction of the Fund, the EU now effectively subsidises the production of military capabilities in line with strict conditionality including a need to co-operate through EU-based consortia based on a minimum of at least two EU states. Under its first call for proposals in December 2021 worth €1.2 billion, the European Commission (2021) received over 140 joint defence project proposals from various member states and industrial partners. Therefore, in the space of 5 years from the creation of the Fund in 2016 to its first call for proposals in 2021, the EU had transitioned from a regulatory actor to a manager of defence projects related to missile interception technologies, modular naval patrol vessels and more.

In this regard, the EDF is indicative of a shift towards industrial policy for defence because the EU now directly intervenes in the European defence market with grants and subsidies. The EDF is therefore an appropriate case study for our purposes due to how it combines questions of defence research, military technology, capability development, regulation, financial incentives and co-operation between EU member states. Arguably, of the suite of EU defence initiatives to emerge since the 2016 publication of the EU Global Strategy, which set the tone for EU security and defence co-operation in the wake of Brexit and the Trump presidency, the EDF is the most far reaching and ambitious. Indeed, at its creation, the Fund was seen as a 'game changer' for EU defence industrial policy because it broke the traditional taboo that forbade the use of the EU budget for defence and military purposes. Today, the EDF is investing approximately €8 billion up to 2027 into defence research and capability development directly from the EU budget. However, even if one acknowledges that questions about geoeconomic security are being pushed to the EU level, there is a need to recognise the continued role of EU member states in shaping the European defence market.

Indeed, neo-functionalism contends that the European Commission has increased its role in EU defence industrial policy by showing creativity with new policy tools such as the EDF (Håkansson, 2021; Haroche, 2020; Sabatino, 2022). However, even neo-functionalist accounts acknowledge that the Commission is limited in its role as a policy entrepreneur because of its 'internal tension between strategic and economic objectives' (Haroche, 2022, p. 14; Interviews 1 and 7). LI takes the opposite view by claiming that EU member states retain their control over EU defence industrial policy due to the sensitivities it poses for national security and economic interests (Calcara, 2019b; Calcara and Simón, 2022; Fiott, 2019b; Hoeffler, 2023). Although the EDF has a legal basis

related to EU competences in research and industrial competitiveness (Fiott, 2020), it also relates to defence capability prioritisation and defence planning, where the member states still retain political control via the treaty provisions on the CSDP. This limits the degree to which the Commission can single-handedly lead on military prioritisation efforts (Interviews 3 and 7), and intergovernmental tools such as the Coordinated Annual Review on Defence (CARD) and the Capability Development Plan (CDP) are still the major sources of capability prioritisation at the EU level (Interviews 2, 4 and 7). Notwithstanding the fact that all 27 member states are represented in the EDF's work programme decision-making framework through programme committees (Brichet et al., 2021), the Fund ultimately fails without the interest and uptake of projects by member states and industries located in the EU (Interviews 3 and 7). Indeed, whilst the EDF committees are chaired by the Commission, each member state is represented on them, which gives governments the opportunity to agree to specific capability projects whilst also giving direction to the EDF's overall direction for military capability development.

Geoeconomics and Relative Gains

In the area of geoeconomics, it is important to weigh up relative gains from an intra- and extra-EU perspective where we can assess the external and internal factors that are driving the industrial policy shift in the EU defence sector. Conceptually understanding any geoeconomic turn in the European defence market presupposes a theoretical lens that is able to (1) capture the political and economic preferences of governments; (2) account for the interplay between national, regional and global economic and security considerations; (3) explain how these governments bargain for European responses to geoeconomic risks; and (4) analyse the role played by EU institutions in developing defence industrial policy. This article contends that insights from relative gains theory and LI can shed light on the balance between *economic and political* and *national and European* factors in the development of EU defence industrial policy. Indeed, relative gains theory helps us recognise that EU member state governments will frame their respective political and economic interests in relation to external factors and how far other EU states will strengthen their position in the Single Market (Simón, 2017).

This may seem like a counterintuitive argument to make given that EU member states are bound by the rules of the Single Market and are part of a Union that is supposed to confer common economic benefits to all its members (Fiott, 2019a). Nonetheless, relative gains theory helps us understand that governments in Europe have to balance considerations of Europe's overall political weight in international politics with the relative intra-European balance of power. Depending on the case, individual European states may forego greater intra-European co-operation if they believe it is likely to imperil their relative international position of power, which remains amplified via the continued hegemonic presence of the United States. In other cases, however, European governments may calculate that their respective national interests are best served by greater intra-European co-operation (Calcara, 2019a; Simón, 2017). This interplay between extra- and intra-European balances of power raises important questions related to any debate about a geoeconomic turn in the European defence sector.

For example, the growing focus on geoeconomics presupposes that manufacturing and productive capacities are a key source of national power (Lind, 2019, p. 12). If this

assumption is correct, then we should expect *relative* rather than *absolute* gains to trump considerations about whether to organise defence industrial policy at the EU level or not. In fact, the scholarly literature on geoeconomics is marked by a transition away from neoliberal understandings of international relations, which relegated security concerns in favour of trade and open markets, towards a greater 'securitisation of economic policy' whereby rules, norms and institutions undergo change to adapt to a need to achieve relative gains in international politics (Roberts et al., 2019). Although scholarly contributions have pointed out that liberalisation at the EU level can mask a strategy of advancing national interests (Hoeffler, 2012; Schilde, 2017), the focus on relative rather than absolute gains also presupposes that states and organisations become more attentive to the vulnerabilities inherent in economic interdependence. Moreover, geoeconomic strategies assume that individual states and international organisations will develop and exercise specific strategies to manage their relative position in world affairs (Wigell, 2016). It is perhaps most important for any account of EU defence industrial co-operation, however, that relative gains are widely seen as a source of competition rather than co-operation (Calcara, 2018; Simón, 2017; Snidal, 1991).

However, whereas relative gains help us better situate the ways in which governments approach questions of relative economic and political power, there is a need to focus on how interests converge and diverge during the development of EU defence industrial policy. As we have seen, EU member states are capable of co-operating on defence industrial issues at the EU level, and this may imply that they have calculated that EU defence industrial co-operation does not overly undermine their relative position within the intra-EU balance of power. It may also imply that EU member states have collectively understood that greater intra-EU co-operation may enhance the Union's relative global position vis-à-vis other international actors. However, to be better able to account for the ways in which governments and institutions organise defence industrial co-operation at the EU level, it is necessary to employ a theoretical framework that can capture the formation of economic interests and bargaining at the EU level.

Bargaining for Defence Industrial Policy

One such obvious, yet contested, theory is LI. Indeed, as a grand theory, LI received prominence in EU integration studies based on the manner in which it underlined the importance of economic preferences and showed how EU governments bargain for policy outcomes. In a bid to push back against neo-functionalism's claim that greater policy spillover can only ever lead to more EU integration, LI showed the ways in which bargains between EU governments could fail or end in compromises that would not necessarily lead to more integration. On top of this, LI claimed that specific structural circumstances would lead to a drive towards bargaining at the EU level in the first place, including globalisation, international competition and states' relative positions in international economic relations. LI also underlined the importance of EU institutions such as the Commission – not as policy entrepreneurs per se but as political bodies that would embed and uphold intergovernmental bargains between EU member states. At least from this perspective, LI can be seen to complement relative gains theory by underlining the specific processes and bargains involved in managing competition and co-operation over EU policy.

However, from a different angle, LI can be seen to contain certain explanatory weaknesses (Kleine and Pollack, 2018). For one thing, in its original incarnation, LI was better suited to explaining bargaining and outcomes for economic domains of EU policy. Indeed, Moravcsik himself avoided using LI to explain European integration in security and defence, even though he started his academic career focusing on armaments co-operation (Fiott, 2019a, p. 17). At first glance, LI is perhaps not best suited to explaining the very interplay between economics and security that appears to characterise industrial policy. Nonetheless, recent scholarly work has shown how LI can indeed apply to the fields of security and defence, and defence industrial policy more specifically (Calcara, 2019b; Fiott, 2019b). Specifically, LI has been updated to help explain the adoption of EU soft law on defence procurement and intra-EU arms transfers, as well as the creation of specialised EU bodies such as the EDA (Fiott, 2019a). What is more, such accounts have confirmed the importance of intergovernmental bargaining relative to the policy agency of institutional actors such as the European Commission, but they have nonetheless stressed the need to treat the Commission as an important variable in government preference formation – not least, as governments seek to manage the control EU institutions can exert over defence industrial policy (Fiott, 2019a).

Under such a reading of LI, it is possible to better understand how governments formulate economic and political preferences. This not only implies that governments must represent national economic preferences but also the preferences of relevant security actors such as relevant government ministries, branches of the armed forces and even allies. Accordingly, the main benefits of combining insights from both relative gains theory and LI are as follows. First, the theoretical frameworks allow for both co-operation and competition in the formulation of EU defence industrial policy. Second, whereas relative gains highlight the tension between intra- and extra-EU balances of power, LI shows in clearer terms how these gains are calculated at a national level and negotiated at the EU level. Third, both theories allow us to understand how governments manage intra- and extra-EU balances of relative power. Coming full circle to the idea of a geoeconomic turn in EU defence industrial policy, both theories appear well suited to explaining the balancing of security and economic interests that are at the heart of geoeconomics.

II. The EDF and the EU's Geoeconomic Turn

As we highlighted earlier, the EDF represents a step change in the way that the Union supports the European defence market because it marks a departure from the regulatory approach that has characterised EU defence industrial policy since its inception. In this section, we assess the Fund from the perspective of intra- and extra-EU relative gains and intergovernmental preferences.

Intra-EU Relative Gains and the EDF

Member states – working through the European Council – were at the heart of agreeing to the Fund, and, without their presence in the working committee and the additional funding they provide for EDF capability projects, the Fund would be unworkable (Interviews 3 and 7). Using relative gains theory and LI, we are able to better understand the modalities under which the member states ultimately agreed to create the Fund. This will

then reveal the factors behind the transition from market liberalisation to industrial policy and allow us to ascertain the reasons behind the geoeconomic turn in EU defence market policy. The first consideration is to analyse how the EDF can be explained in relation to intra-EU relative gains. Clearly, the fact that the European Council and member states were open to the idea of a fund shows that intra-EU relative gain considerations could be effectively managed. This was not a foregone conclusion given how fragmented the European defence market is and how defence industrial production is highly concentrated in the hands of only a few larger EU member states. In this sense, the EDF would have been much harder to create and justify as an EU policy if it was perceived to be a funnel for EU funds into the hands of only a few member states.

On the face of it, one could argue that the EDF has so far only really benefited a minority of the larger member states. The data available for the precursor programme to the EDF – the so-called European Defence Industrial Development Programme (EDIDP) – show that in 2020, 21% of overall beneficiaries were from France, 12% from Spain, 12% from Italy and 9% from Germany (Masson, 2021). Yet, there are several ways in which smaller and medium-sized member states gain from the EDF. Indeed, their industries can directly benefit from being part of project consortia with larger industrial actors. This has the benefit of potential knowledge and technology transfer, as small- and medium-sized enterprises (SMEs) are exposed to intricate industrial processes that can help their own competitiveness. This is a particularly important, yet under-appreciated, feature of the Fund. Smaller and medium-sized member states can help their own nascent defence industries plug into European supply chains, and a critical part of the Commission's stewardship of the EDF is to ensure the access of SMEs to projects and cross-border supply chains (Interview 6).

By directing us to focus on national preference formation and EU-level bargaining, LI helps us understand the ways in which EU member states reconciled their defence industrial interests through the EDF. For France, the EDF was viewed as a major step towards ensuring additional financial and political support for the European defence market, which it has a large stake in. Not only was French industry behind the drive towards more financial support for defence research and capability development (Interview 5), but the government seized on a 'window of opportunity' during the height of the Brexit crisis and the Trump presidency to call for policies such as the EDF (Béraud-Sudreau and Pannier, 2020). France was joined by Germany, where the defence industry was also interested in using common EU financing to support its own defence modernisation and ensure common action to develop capabilities for both the EU and the North Atlantic Treaty Organization (NATO) (Major and Mölling, 2019; Interview 4). Other major defence industrial countries such as Spain and Italy also saw the EDF as beneficial for their national industries: Spain saw the Fund as an opportunity to support and rationalise its own defence industrial base (Arteaga, 2019), and Italy stressed that the Fund would lead to joint defence programmes that would boost European strategic autonomy (Marrone, 2019).

There were also states that feared the EDF would sever links with the American and British defence markets and/or that the Fund would empower a French–German defence industrial concentration. Sweden, another major European defence market, was one such country that had concerns that the EDF could be used to break industrial linkages with American and British firms (Olsson, 2019). Yet, Sweden and other states did not ultimately object to the Fund's creation. Countries such as Poland saw the EDF as a solid

opportunity to develop military capabilities that would be of value in a NATO setting, but it also saw a strong vested interest in being part of the EDF for the purposes of technology and knowledge transfers. As one analyst put it, 'Poland expects the EDF to allow Polish defence companies to finally join European defence industrial cooperation' by helping to support its mid-sized firms and the large concentration of companies under the Polish Armaments Group (PGZ) (Terlikowski, 2019, p. 3). Finland also took a pragmatic view of the EDF, and its industry saw the benefits of the economic opportunities that would be possible from cross-border defence supply chains, especially for a country that had traditionally relied on off-the-shelf purchases and highly specialised technology manufacturing (Helwig and Iso-Markku, 2020).

Thus, the underlying political logic of the EDF is a careful balancing of relative gains where larger and smaller EU states receive public goods from a financing mechanism that is regulated at the EU level. In this sense, there is something to LI's claim that the European Commission's role is as much about managing the political bargain reached between member states as serving as a policy entrepreneur. In this sense, if the original bargain between governments over the EDF is to hold over time, the Commission and the European Parliament must ensure that the benefits from co-operation (however 'benefits' are ultimately defined) are fairly apportioned. This is perhaps a more delicate issue than we may initially appreciate. Consider, for example, how the EDF melds with the politics of the EU budget: net contributors to the budget insist that they receive a larger share of EU investments, whereas net beneficiaries do not want to see their financial contributions being used to finance already competitive defence industries (Interview 8).

Furthermore, the political bargain achieved for the EDF must be seen as part of a wider political bargain involving member states through Permanent Structured Cooperation (PESCO). Indeed, member states were successful in establishing a direct link between the EDF and PESCO, which is a wholly intergovernmental EU defence capability policy framework. Like the EDF, PESCO projects are designed to fill military capability gaps in Europe, but political control of PESCO projects resides with the Council of the EU working through the EDA, the EU Military Committee and the European External Action Service (EEAS). Interestingly, several of the ongoing technologically advanced EDF projects are also classed as PESCO projects, which raises a governance question of who ultimately governs a capability project if it is simultaneously developed under the EDF and PESCO. In this respect, it has been argued that larger member states have used PESCO to pre-position projects for EDF funding and that, ultimately, PESCO–EDF projects allow national governments to underline their political primacy over the Commission (Interviews 2 and 7).

Extra-EU Relative Gains and the Transatlantic Dimension

So far, relative gains theory and LI have helped us better understand the political dynamics at play in negotiating and establishing the EDF. However, the analysis up to now has focused on the management of intra-EU dynamics of relative gains, and an equally important element to concentrate on, especially with regard to any geoeconomic turn, is extra-EU relative gains. Managing relative gains between the EU and international competitors not only raises the importance of geoeconomic competition but also underlines the importance of structural pressures such as the 'weaponisation' of economic

dependencies, technology control and security of supply. In other words, it is necessary to understand how governments calculated relative gains in terms of the global balance of power, especially in relation to European relations with the United States, which has always had a bearing on EU defence industrial policy. In addition unpacking the structural influence of transatlantic defence market competition there is a need to understand what factors undergirded the political necessity of the EDF.

With specific reference to the United States as a structural factor in EU defence industrial policy, the EDF is a puzzling creation because pressure from the United States has existed for several decades. Steps by successive US administrations to maintain open European defence markets and thus to ensure the competitiveness of US defence firms in Europe did not lead to a shift from regulation to the EDF before. Therefore, it is necessary to understand what specific conditions in the transatlantic relationship gave rise to the EDF. A significant explanation in this regard was the Trump administration, which re-aligned its own geoeconomic strategy towards a more nationalistic and China-focused approach that called into question the long-standing economic relationship with the EU. Added to this development was the specific defence policy stance of the Trump administration to NATO and European security, with warnings from the president that the United States could potentially leave NATO or not meet its responsibilities for collective defence under Article 5 of the Washington Treaty. Again, this was largely read as a US downgrading of Europe in Washington's overall grand strategy towards rivalry with China (Simón et al., 2021). To be sure, calls for Europeans to do more for their security from the United States are not new, but the prospect of a sitting US president being responsible for the wholesale deterioration of the NATO alliance had a seismic effect on how European governments viewed defence co-operation through the EU.

In this sense, the EDF became an important symbol of European governments seeking to hedge against perceived shifts in US policy. This manifested itself in calls for a financial tool that would help lead to the development of EU-made military capabilities and European supply chains that would be resistant to US extra-territorial legislation such as the International Traffic in Arms Regulations (ITAR). Again, the risk that the United States could block exports or condition the use of European-owned military capabilities pre-dates the creation of the EDF, but it was unclear at the time how the Trump administration would instrumentalise US law to further benefit the US defence industry. In this sense, Europe has used its fear of structural factors to develop ways of ensuring supply chain security. Accordingly, the crisis in transatlantic relations at the time posed a major dilemma for European governments. For past crises such as the Arab Spring, the Balkan Wars or the Ukraine crisis, the United States has had a unifying effect on European governments, which has helped manage intra-EU political dynamics (see Haroche, 2017). However, the Trump administration became the object of the crisis itself, spurring European governments to resolve their intra-EU defence dynamics on their own.

Interestingly, even after EU member states decided to create the Fund, many governments resisted US attempts to open up the Fund to American defence producers (Interview 9). The very fact that the United States would try to open up the EDF to American producers after calling for Europeans to do more for their own defence hints at how sensitive the move to create the EDF was in transatlantic relations. Indeed, at the time, the launch of the EDF and PESCO was likened by the then-Trump "administration to 'poison pills'" that would distort existing transatlantic defence supply chains (Interviews 8 and 9).

Despite a very public outcry by the United States through a direct letter to the then High Representative (HR)/Vice-President (VP), Federica Mogherini, which called for the EU to open up the EDF to American firms, the Union held to its position of creating a fund that was legally and politically closed to American and other non-EU firms (Fiott, 2019b). In this sense, one is able to conclude that European governments successfully balanced extra- and intra-EU political dynamics in such a way as to protect their national interests, whilst shielding the EU from the potential risks of the Trump presidency.

Of course, the introduction of the EDF did not sever all transatlantic defence industrial ties, and in hindsight, the US reaction was perhaps overblown (Interview 8). The reality today, which the European response to the war on Ukraine has emphasised, is that Europeans still maintain a high degree of dependence on US armaments. Nonetheless, the aggregate of national preferences during the negotiations for the EDF during the Trump presidency led member states to ring-fence their defence industrial efforts from external influence and competitors. They did so in such a way as to benefit their national defence firms, whilst also trying to cushion any perceived hostile action by Europeans to the transatlantic relationship. Member states did not want to give President Trump any ammunition for his hostility towards NATO and European security. It is for this reason that the EDF began as a relatively small-scale financial tool worth €8 billion. In fact, the Finnish Presidency of the Council of the EU in 2019 oversaw a reduction of the Fund from an initial Commission request of €13 billion to €8 billion, which was seen as a way to assuage voices in the United States that it was the Europeans rather than America that sought decoupling.

Despite its relatively small size, however, the EDF was also seen as a way to develop military technologies and capabilities that could be shielded from the reaches of US extra-territorial legislation such as ITAR, which can control and block the military technologies of allied and non-allied countries alike. Indeed, the way the EDF Regulation has been drafted leaves little room for non-EU states to control EU-developed defence technologies. As Article 20(3) of the Regulation stipulates, 'the results of research actions supported by the Fund shall not be subject to any control or restriction by a non-associated third country […] including in terms of technology transfer' (EU, 2021). Although certain EU member states such as Sweden raised objections about this technology protection provision (Interviews 1 and 7), overall, the EU member states settled on a legal basis that would shield any EU-funded defence research and capability efforts from US and other non-EU legislation. In this sense, the shift in US strategy under Trump presented the Europeans with an opportunity to develop 'ITAR-free' military equipment, which is seen as a vital part of the European ability to export military equipment.

In terms of geoeconomics, this would appear to be an interesting case of where the EU sought to balance economic and security considerations, and it is certainly interesting that, despite protests from Washington, member states continued to pursue technology security guarantees in the EDF. Such a step fits with the Union's overall drive towards achieving 'strategic autonomy' in defence (see Juncos and Vanhoonacker, 2024, this issue). Given President Trump's aim to compete with the EU in terms of trade – with the president even calling the EU a 'foe' in trade (Roth et al., 2018) – states such as France and Germany were eager to ensure that the EDF could be used to enhance EU autonomy (Interviews 4 and 5). In this sense, there was an intimate link between intra- and extra-EU relative gains, with larger industrial countries such as France, Germany, Italy and Spain seeking

to protect their relative position in the European defence market by shielding the Fund from external technology controls by the United States and other non-EU countries. Whereas under the Union's past regulatory approach, non-EU defence firms still enjoyed access to the European defence market (Fiott, 2019b), the Fund became a feature of EU industrial policy with financial incentives and legal safeguards for EU member states.

In the context of our theoretical discussion, the case of the EDF raises noteworthy observations about how member states balanced relative gains. On the one hand, they were able to manage intra-EU relative gains considerations by ensuring that the Fund would meet various economic preferences such as providing additional financial support from the EU budget for defence, technology sharing and support for SMEs. EU law and institutions such as the European Commission played the role of locking in this EU-level bargain. Whilst there has been a traditional scepticism about the durability of intergovernmental armaments collaboration (DeVore, 2014), the Fund marks an interesting and innovative approach to defence industrial co-operation as it seeks to harness the Union's supranational architecture to better manage potential conflict between member states as to how the Fund should be invested and where. On the other hand, the Fund is not just a case of managing intra-EU defence industrial preferences as it also speaks to how EU member states view their relative position vis-à-vis global industrial powers such as the United States. Remarkably, and despite political pressure from the United States during the creation of the Fund, member states agreed on a legal framework for the Fund that essentially underlined the importance of maintaining a European defence market and boosting its competitiveness in relation to other global defence actors.

Conclusion

At the start of this article, we set out to analyse whether the European defence market could be said to reflect a 'geoeconomic turn'. The article first clarified the term 'geoeconomics' by highlighting how it marked a transition from absolute economic gains to relative gains: in essence, any geoeconomic turn implies that governments and institutions balance economic and security interests. However, this article showed how this definition of geoeconomics is complicated in an EU context, as governments not only have to balance security and economic preferences but also need to calculate the trade-off between intra- and extra-EU relative gains. Drawing on the specific case of the EDF, this article has been able to show how governments formed and balanced their security and economic preferences in an EU context. Specifically addressing the research question, the article has shown how the EU has moved away from its traditional drive towards market liberalisation by establishing a fund that exhibits strong elements of an industrial policy for defence consisting of direct market intervention through financing and subsidies. This process is likely to increase in the future, especially as the Union will release its first Defence Industrial Strategy in early 2024 with the aim of introducing further political direction for the European defence industry.

Drawing on both relative gains theory and LI, the article has been able to demonstrate how national preferences were embedded in the EDF. This article has shown that the EDF embodies the industrial interests of member states and reflects a careful calibration of the interests of large, medium and small member states. However, the study of extra-EU gains has revealed that the EDF was a response to a specific structural pressure on the EU posed by the

United States. To be sure, EU defence industrial policy has also been influenced by the transatlantic relationship, but at the time of the EDF's creation, the Trump presidency posed specific political considerations such as the risk of US decoupling from European security and heightened economic competition. In this sense, member state governments were responding to important shifts in US geoeconomic policy and strategy by ensuring that EU financial tools could support an EDTIB. The fact that the member states that are traditionally close to the US defence market were unable to block the EDF's creation or remove provisions that locked out US firms from the Fund is telling. Although defence market competition from the United States has always been a justification for the EU's own defence industrial policy, a shift to a more nationalistic and competitive geoeconomic strategy in the United States played a major role in the creation of the EDF, as well as pushing the EU towards industrial policy rather than further market liberalisation in the defence sector.

This special issue sets out to analyse various areas of EU policy through the lens of geoeconomics. It usefully initiates a research agenda that can help probe how the EU balances economic and security interests in its policy: given the growing global geostrategic rivalry, this is a timely and important endeavour. As a direct response to the main theme of this special issue, this article has provided some preliminary explanations for why the EU has taken a geoeconomic turn in the defence sector marked by industrial policy rather than market liberalisation. We argue that a theoretical combination of relative gains and LI has helped us explain how the EDF, a landmark example of EU defence industrial policy, was created and how the structural considerations helped mould intra-EU dynamics. Future research should continue to test this theoretical approach in light of the policy changes introduced since the Versailles Summit of March 2022 (European Council, 2022). Such changes include calls for more EU action on joint defence procurement and common EU-level defence planning (European Commission, 2022, p. 14). Greater common EU defence planning would itself be a revolutionary step forward for the Union, and so it would be necessary to further investigate how the balance between intra- and extra-EU relative gains and domestic security/economic preferences evolves over time.

Furthermore, another fundamental aspect of any future research agenda on the EU and geoeconomics should focus more intensely on the linkages between new EU policies (as called for in this special issue by Herranz-Surrallés et al., 2024). There is an interdependence between EU defence industrial policy and Union initiatives in the areas of semiconductors, critical raw materials, outer space and more. In this sense, one of the theoretical and empirical deficiencies of this article is how national preferences in defence are influenced by preferences related to wider areas of EU technology policy and digital policy. For example, the 'EU Chips Act' or the EU's Foreign Direct Investment (FDI) Screening Mechanism has an essential bearing on the EU defence market, and it is worth studying the specific balance between national preferences when all these new policy areas are compared. In this respect, it is also interesting to study to what extent structural factors have conditioned developments in these new geoeconomic areas of policy. When taken together, these factors could usefully provide a comprehensive account of the EU's geoeconomic actorness.

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Interviews

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Interview 3: Official, European External Action Service, 25 November 2022.
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Interview 5: Official, Government of France, 18 November 2022.
Interview 6: Official, European Commission, 2 November 2022.
Interview 7: Official, European Defence Agency, 7 November 2022.
Interview 8: Official, European Commission, 26 October 2022.
Interview 9: Official, European Commission, 15 November 2022.